STABILIZING THE DOLLAR

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Monetary Standards throughout the world have been disrupted by the war. Inflation in various forms, such as paper-money inflation and bank-credit inflation among the countries at war, and gold inflation among other countries, has everywhere caused a depreciation of monetary units. Consequently we have high prices the world over, even where there is no scarcity of goods. Already, before the war, there was world-wide complaint of the high cost of living, but the rise in this country before 1914 was small compared to what it has been since. Between 1913 and 1918 prices had increased 107 per cent; whereas between 1896 and 1913 the increase was only 50 per cent.

Prior to 1896, partly because of a disproportion between the increase in the amount of currency and the more rapid increase in the demands of business, there had been a decrease in the price level. This had caused as much complaint as the present rising prices. The situation had become so serious that various alleged remedies were suggested to stop or offset the fall.

As to the future, the general expectation seems to be of a decline in prices, which would, however, if sharp, be just as great an evil as the present high prices. A rapid contraction of the currency would be a grave danger in times of reconstruction. A fall in prices (or appreciation of the dollar) would put a heavy burden on the debtor, who must repay so much more than he borrowed. However, this fall is not certain, and the very uncertainty is itself an evil.

The truth is, the purchasing power of the dollar and other monetary units has always been and, until some radical remedy is applied, always will be unstable. The dollar is, to be sure, stable in weight, for, by definition, it is 25.8 gr. of gold, 9/10 fine. But, for that very reason, it fluctuates in value-in-exchange, according to the various forces affecting gold and the various forces affecting the volume of currency, such as methods of gold mining, changes in the use of credit, and so on. Other units, the pound, the yard, the bushel, once fluctuated as the "unit of value" now does, but with the progress of civilization, they have, one after another, been standardized. Our unstable and unstandardized

monetary units are among the last remnants of barbarism and are out of place in present-day civilization.

The fundamental reason why the dollar has not hitherto been standardized in value is that only within a generation have we had the means of measuring its value. Before the pound weight could be stabilized, scales had to be invented, and before any other units could be stabilized, the proper instruments for measuring them had to be devised. For measuring changes in the price level we now have the "index number" of prices.

This use of the index number would carry one step further the transition in our conception of money which began with the Bullion Report. At that time, the public was educated up to the point of recognizing gold as the standard for measuring paper money, although in the market paper was the standard in terms of which the price of gold was recorded. But it still remains to grasp the concept of measuring gold in goods instead of, as at present, goods in gold. It is as great an advance in thought to think in terms of goods instead of in terms of gold as it was, a century ago, to think in terms of gold instead of in terms of paper. Whether, in the future, we shall find a still more absolute standard of value need not concern us now. The point is that we now have, in the index number, a means of measuring gold appreciation and depreciation in terms of goods.

In connection with the proposal to stabilize the dollar, two main questions need to be asked: (1) At what price level do we want to start a stable dollar? (2) How can that price level be kept?

In regard to the first question, the present price level is so abnormally high that it seems doubtful wisdom to launch a plan which would fix the dollar at its present low purchasing power. At the same time it would be absurd to go back to 1896, the low-water mark of prices, for the debts existing then have almost all been paid and wages and salaries have become adjusted to a higher level. We can not now do justice to all those who suffered by past price movements. The chief object of stabilization is to provide a stable yardstick for contracts to serve future generations of business. Next in importance is the object of preventing injustice, in the immediate future, to those who are now debtors or creditors or who would otherwise be affected by any impending unforeseen fluctuation in monetary standards. It may, therefore, be necessary to endure some injustice, at the time of inaugurating the new plan, for the sake of bringing about the ultimate reform,

but by a careful study of existing contracts, practical justice can be attained.

Most existing contracts and understandings were made during the war. A rough estimate which I have made of existing indebtedness—bonds, notes, mortgages, bank loans, and other obligations—seems to indicate that their average duration is approximately two years. If then the price level should soon become what it was two years ago, say in 1916-17, it would seem wise to adopt that level as the start-off.

As to the second question, how to keep this price level, or in other words, how to stabilize the dollar, there may be other solutions than the one I have been active in advocating. The important point is to find *some* solution. The evils of an unstable dollar are intolerable. The solution of the problem is one of the tasks of reconstruction. One of the simplest and yet one of the greatest reforms that we economists can advocate is this one. It is as simple as daylight saving, and a million times as important. Stabilizing the dollar affects not simply money, but relates itself to the whole question of the distribution of wealth and to labor unrest. The disproportion between the level of wages and the soaring price level has, for instance, been responsible for much of the recent labor agitation.

The particular plan which I am about to discuss is somewhat associated with my name, but I am not its sole author. It was worked out independently before me, in some detail, by Aneurin Williams, M. P., Professor (now Dean) Smith of the University of Washington, D. J. Tinnes of Hunter, N. D., and Henry Heaton of Atlantic, Iowa; and in its general idea, by President Woodrow Wilson, Simon Newcomb, Alfred Russel Wallace, Professor Alfred Marshall, William C. Foster of Watertown, Mass., and others.

Briefly, this particular proposal is to shift the weight of the dollar (or the amount of gold bullion exchangeable for a gold certificate) up or down according as the purchasing power of the dollar (as measured by the index number of prices) goes down or up. Thus the purchasing power of the gold certificate will be kept constant in terms of goods while the weight of the gold dollar is allowed to fluctuate.

I shall assume that the plan, in a general way, is understood.[1]

[1] See *American Problems of Reconstruction* (E. P. Dutton & Co., 1918); article by Irving Fisher, "Stabilizing the Dollar in Purchasing Power"; and forthcoming book by same title, to be published by Macmillan.

None of the technical difficulties in such a plan is in any way serious. I shall refer to only a few of them.

First, as to the gold reserve behind the proposed gold certificates or, as they would better be called under the new system, the gold dollar certificates. If the gold dollar certificates outstanding are now equal, dollar for dollar, to the gold in the Treasury, but next month, because of a change in weight of the dollar, they call for one per cent more gold, must the Treasury find the additional bullion and if so how? It would, of course, be perfectly possible (though not necessary) to maintain, as at present, a 100 per cent reserve against these certificates, the government making up the deficit when gold depreciated, perhaps through taxation. If, on the other hand, gold were appreciating, the government would reap a profit. This gain and loss, however, are not really new phenomena resulting from stabilizing the dollar. They exist today. But, under our present system, the loss (or gain) falls on the individual holder of gold certificates instead of on the government. Stabilizing the dollar simply affords a specific measure of this loss, if it be a loss, and maintaining the reserve translates that loss into taxes.

It would be more simple, however, to allow the reserve gradually to fall below par, say, to 50 per cent, before replenishing the supply of bullion. Any surplus above this 50 per cent which might exist at a time of falling prices or decreasing dollar weight could be put to work to earn interest which would to a large extent provide against loss when prices began to rise again. This could be done by investing this "surplus" in government bonds.

A second technical point in the plan is the choice of the index number which is to be the basis of the changes in the "dollar-weight." Although the method of computing the index number has surprisingly little effect in general on the resulting figures, nevertheless differences do appear; and it is therefore worth while to construct an index number as nearly perfect as possible. The main factors are the markets from which prices are collected; the kind of prices, that is, wholesale or retail; the list of commodities included; the frequency of calculation; and the formula for calculation.

For the first, the markets should be the chief public markets of the United States such as those now used by the United States Bureau of Labor Statistics, and the prices should be secured through government agents and trade journals.

I am at present rather inclined to think that wholesale prices should be used, first because of the greater ease they offer in standardizing certain grades of goods, and secondly because of their greater sensitiveness to the influences which affect price levels. This second reason is illustrated by the contrast between street-railway fares, which remained the same through two decades of price upheavals which affected all other prices, and silver, which is rarely quoted the same on two successive days.

This same consideration is important in selecting the list of commodities, which should exclude the sluggish commodities in order to be promptly responsive to price changes. I have had an index number of such responsive commodities calculated through the help of Mr. Bell of the Bureau of Labor Statistics, and it shows a rise greater and prompter since 1914 than that of the regular index number, including, as it does, sluggish and price-fixed articles.

I believe that, if wholesale prices are stabilized, retail prices will also be stable. The present discrepancy between the movement of retail and wholesale prices is due to the lagging behind of the retail prices whenever the wholesale prices move more swiftly up or down. But there can be no lagging behind when prices are stable. I am much gratified, however, as well as surprised, to learn that Commissioner Meeker has worked out a satisfactory index for cost of living based on retail prices. This should certainly be used for wage adjustment, so long as we have no stabilization of money.

The frequency of calculating the index number (which means the frequency of adjusting the dollar weight) depends on the time required to calculate an index number and that required for such an adjustment to be felt. Judging from the rapidity with which some of the commercial index numbers are calculated and published, I believe an index number could easily be calculated within two or three days after the date for which the prices are quoted. How quickly the index number responds to a change in the monetary supply has never been fully demonstrated. A lag of from one to three months is most probable.

So much for some of the points of this particular plan.

There are a number of other details which will have to be considered when, if ever, this plan comes up for legislative adoption and which will be treated in my book. But those which have been mentioned are those of most importance.